

Message Text

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ACTION TRSE-00

INFO OCT-01 EA-06 ISO-00 AID-05 CIAE-00 COME-00 EB-07

FRB-01 INR-05 NSAE-00 RSC-01 XMB-02 OPIC-03 SP-02

CIEP-01 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-01

CEA-01 /062 W

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R 240310Z DEC 74

FM AMEMBASSY TOKYO

TO SECSTATE WASHDC 6931

LIMITED OFFICIAL USE SECTION 1 OF 2 TOKYO 16689

PASS TREASURY/OASIA FOR WIDMAN

E.O. 11652: N/A

TAGS: EFIN, JA

SUBJECT: ECONOMIC FORECAST FOR JAPAN 1975

SUMMARY: IN ANSWER TO SPECIFIC TREASURY REQUEST, FOLLOWING IS FINATT'S BEST ESTIMATE OF JAPAN'S PROSPECTS FOR CY 1975. CURRENT GOJ ECONOMIC POLICY AND BUDGET MAKING HAVE NOT YET BEEN FINALIZED. HOWEVER, PRESENT AUSTERITY PROGRAM WILL PROBABLY BE CONTINUED FOR NEXT TWO QUARTERS UNTIL 1975 "WAGE OFFENSIVE" HAS BEEN SETTLED. AT THAT TIME, OUTLOOK FOR PRICE/WAGE STABILITY MAY HAVE IMPROVED SUFFICIENTLY TO PERMIT RELAXATION OF TIGHT MONETARY POLICY AND ACCELERATION OF GROWTH RATE. NEVERTHELESS, GOJ APPEARS TO RULE OUT POSSIBILITY OF RETURNING TO 8-10 PERCENT HIGH GROWTH RATES OF THE PAST. FOR CY 1975 FINATT PROJECTS 3 PERCENT REAL GNP GROWTH ALONG WITH CURRENT ACCOUNT EQUILIBRIUM (WHICH HAS BEEN SITUATION IN PAST FEW MONTHS). THUS FUKUDA'S B/P OBJECTIVES (AS MENTIONED TO FORMER SEC SHULTZ IN KUALA LUMPUR) ARE LIKELY TO BE ATTAINED AS A RESULT OF POLICIES AIMED AT ACHIEVING PURELY DOMESTIC OBJECTIVES OF GREATER INTERNAL ECONOMIC STABILITY. END SUMMARY.

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1. OVERVIEW: DIR GEN OF EPA FUKUDA TAKING STRONG INITIATIVE AS CHAIRMAN OF NEW COUNCIL FOR ECONOMIC POLICY (CEP) IN FORMULATING ECONOMIC AND BUDGET STRATEGY FOR NEXT FISCAL YEAR (TOKYO 16,153). FINAL POLICY AND OFFICIAL PROJECTION WILL BE KNOWN WITHIN ABOUT TWO WEEKS. GENERAL CONSENSUS(EVEN AMONG BUSINESSMEN) IS THAT PRIORITY MUST BE GIVEN TO PRICE STABILITY SO AS TO MINIMIZE WAGE INCREASE TO BE NEGOTIATED IN MARCH-APRIL "WAGE OFFENSIVE." CONSEQUENTLY, FINATT FORESEES "STAND-PAT" MONETAR FISCAL POLICY AT LEAST UNTIL MID-YEAR. IF AT THAT TIME PRICE RISE HAS DROPPED TO ANNUAL RATE OF 10 PERCENT OR LESS FOR CPI AND WAGE SETTLEMENT IS NO MORE THAN 15 PERCENT INCREASE FOR PAST INFLATION PLUS 5 PERCENT FOR "PRODUCTIVITY ADVANCE" (I.E. TOTAL INCREASE OF 20 PERCENT) GOJ MAY BEGIN TO EASE PRESENT AUSTERITY POLICY. BY THAT TIME FUKUDA MAY HAVE EVOLVED NEW MEDIUM-TERM ECONOMIC PLAN AND A GENERAL CONSENSUS ON APPROPRIATE FUTURE RATE OF GROWTH OF REAL GNP. PROBABLE POLICY REVIEW IN EARLY SUMMER COULD HAVE STRONG INFLUENCE ON ECONOMIC OUTTURN IN CY AND JFY 1975. THEREFORE, FINATT PROJECTS REPRESENT ONLY IMPLICATIONS OF LIKELY DEVELOPMENTS AS SEEN AT THIS TIME.

2. CURRENT SITUATION: UNLIKE PREVIOUS RECESSION PERIODS, CUTBACK IN REAL CONSUMER SPENDING (DESPITE INCREASE IN REAL INCOME SINCE ABOUT MID-YEAR) HAS CREATE PRESENT UNEXPECTED GLUT OF INVENTOIRES. THERE IS GENERAL CONVICTION THAT STOCKS WILL BE WORKED OFF AND PRODUCTION RATES WILL AGAIN RISE AS SOON AS CONSUMERS RESUME SPENDING AND REDUCE PRESENT HIGH SAVINGS RATES. FINATT BELIEVES PRESENT PRECAUTIONARY SAVINGS INCENTIVE MAY BE SUSTAINED FOR SOME TIME IN VIEW OF DETERIORATING LABOR MARKET AND EMPLOYMENT CONDITIONS. MOST WORKERS REPORTEDLY BEING "FORCED" TO SAVE EVEN YEAR-END BONUS PAYMENTS, AS COMPANIES SHORT OF CASH ARE OFFERING 10 PERCENT INTEREST TO WORKERS WHO DO NOT REQUEST PAYMENT BUT KEEP FUNDS ON DEPOSIT WITH COMPANY. MOREOVER, RECENT NEW ORDER STATISTICS SUGGEST UNEXPECTED WEAKENING IN FUTURE PLANT AND EQUIPMENT INVESTMENT. THEREFORE, STRINGTH OF REAL DOMESTIC DEMAND WHICH IS BEING RELIED UPON TO REVIVE ECONOMY REMAINS UNCERTAIN DURING THE NEXT LIMITED OFFICIAL USE

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SEVERAL MONTHS.

3. EXTERNAL SITUATION: INVENTORY BUILDUP ON 1974 HAS HAD DRAMATIC IMPACT ON EXTERNAL SURPLUS THROUGH EXPANSION OF EXPORTS AND CUTBACK IN IMPORTS (SEE TOKYO 16,173). REEMERGENCE OF VERY LARGE REAL EXTERNAL SURPLUS (NATIONAL ACCOUNTS BASIS IN CONSTANT PRICES) EQUIVALENT TO 2.7 PERCENT OF GNP IN THRID QUARTER (SAME PROPORTION

AS IN CY 1972 AND 73) SUGGESTS THAT JAPAN'S REAL PRO-
PENSITIES TO IMPORT AND EXPORT REMAIN BASICALLY UNCHANGED
FROM EARLIER PERIODS DESPITE CHANGE IN EXTERNAL ENVIRON-
MENT AND COMPETITIVE SITUATION DURING PAST 3 YEARS.
ECONOMETRIC EQUATIONS USED IN PAST TO EXPLAIN EXPORTS
AND IMPORTS CONTINUE TO PERFORM WELL ACCORDING TO
KNOWLEDGEABLE JAPANESE ECONOMISTS. VERY LARGE DETERIORA-
TION IN TERMS OF TRADE (23 PERCENT FROM 1972 TO THIRD
QUARTER 1974 ON BASIS OF GNP IMPLICIT PRICE DEFLATORS
AND 28 PERCENT ON BASIS OF BOJ EXPORT AND IMPORT PRICE
INDICES) IS FACTOR WHICH HAS LIMITED IMPROVEMENT OF
BALANCE OF PAYMENTS ON CURRENT ACCOUNT DESPITE REBUILD-
ING OF REAL EXTERNAL SURPLUS (NATIONAL ACCOUNTS BASIS).
FUTURE B/P PROSPECTS DEPEND HEAVILY ON ASSUMPTIONS
ABOUT REAL GROWTH RATES IN JAPAN COMPARED WITH REST OF
WORLD, AND WHETHER JAPAN'S TERMS OF TRADE WILL IMPROVE
OR CONTINUE TO DETERIORATE.

4. PROJECTION: CURRENT PROJECTION DOES NOT DIFFER
DRASTICALLY FROM MOST RECENT OECD PROJECTION. JAPAN'S
GNP STATISTICS FOR LATE 1973 AND EARLY 1974 ARE IN PRO-
CESS OF REVISION SO THAT VALUES FOR CY 1973-74 CITED
BELOW WILL ALSO BE SUBJECT TO SLIGHT CHANGES. GNP
REVISIONS WILL, HOWEVER, BE TAKEN INTO ACCOUNT IN THE
OFFICIAL GOJ PROJECT JFY 1975 TO BE RELEASED SHORTLY.

(A) GNP - ACCORDING TO PRESS REPORTS CEP HAS AGREED
DEC 21 ON 4 PLUS PERCENT REAL GROWTH RATE OBJECTIVE
FOR JFY 1975. FINATT BELIEVES SUCH RATE IS REASONABLE POLICY
TARGET. GROWTH OF ONLY 2 PERCENT OR 3 PERCENT JFY 75
IMPLIES CY 1975 GROWTH RATE OF ONLY 1.8 AND 2.4
PERCENT RESPECTIVELY. THESE WOULD PROVIDE LITTLE IF
ANY PRODUCTIVITY ADVANCE AND MERELY EXACERBATE COST/PUSH
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PROBLEMS WHICH GOJ SEEKING TO CORRECT (UNIT LABOR COSTS IN SEPT
ALREADY UP 36 PERCENT OVER THE YEAR). USING EPA
ASSUMPTIONS OF REAL GNP GROWTH OF 0.5 PERCENT AND 1.0
PERCENT FOR CURRENT AND NEXT QUARTER, AND ASSUMING STEADY
QUARTERLY RATE OF INCREASE DURING JFY 1975, REAL GNP WILL
RISE BY 3.0 PERCENT IN CY 1975 IF JFY 1975 GAIN IS 4.0
PERCENT. THE PREVIOUS PEAK IN REAL GNP (LAST HALF OF
1973) WILL BE REACHED IN THE THIRD QUARTER OF 1975.
REMAINDER OF FORECAST IS AS FOLLOWS:

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ACTION TRSE-00

INFO OCT-01 EA-06 ISO-00 AID-05 CIAE-00 COME-00 EB-07

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R 240310Z DEC 74

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CY 1974 CY 1975 IV 75/

ESTIMATE FORECAST IV 74

REAL GNP MINUS 3.1 3.0 4.7

CIP 25 14

IMPORTS - QUANTUM INDEX MINUS 1.0 4 18.2

DOLLAR VALUE 62.5 13.4

IMPLIED PRICE INDEX 64.1 9.0

(MOF UNIT VALUE INDEX) (78.3)

EXPORTS -QUANTUM INDEX 16.5 9 3.0

DOLLAR VALUE 50.7 21.5

IMPLIED PRICE INDEX 29.4 15

(MOF UNIT VALUE
INDEX) (39.7)

(B) BALANCE OF PAYMENTS - IN THE LAST THREE MONTHS (SEPT-
NOV) THE SEASONALLY ADJUSTED QUANTUM INDEX FOR IMPORTS
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WAS 6.3 PERCENT BELOW THE AVERAGE MONTHLY VALUE FOR 1974. HOWEVER, EVEN IF THE VOLUME OF IMPORTS IN CY 1975 IS UP ONLY 4 PERCENT OVER CY 1974, THE INCREASE OVER THE FOURTH QUARTER OF THIS YEAR WILL BE OVER 18 PERCENT ASSUMING A SMOOTH GROWTH OVER THE YEAR. ON THE OTHER HAND, THE QUANTUM INDEX FOR EXPORTS IN PAST THREE MONTHS WAS UP 6.3 PERCENT OVER THE AVERAGE MONTHLY VALUE FOR 1974. A PROJECTED ANNUAL INCREASE OF 9 PERCENT FOR CY 1975 AS A WHOLE IMPLIES AN INCREASE OF ONLY 3 PERCENT FROM THE FOURTH QUARTER TO FOURTH QUARTER 1975. THESE RESULTS WOULD NOT BE REACHED IF AT MID-YEAR GOJ POLICY WERE ALTERED. THE PROJECTED CHANGES IN THE VOLUME OF BOTH IMPORTS AND EXPORTS FOR CY 1975 ARE SLIGHTLY LARGER THAN THOSE ESTIMATED BY THE OECD, ALTHOUGH PROJECTED DOLLAR VALUES OF TRADE ARE MUCH CLOSER. FINATT ANTICIPATES A SOMEWHAT LARGE TRADE SURPLUS THAN OECD AND EQUILIBRIUM ON CURRENT ACCOUNT. THE IMPLICATION IS THAT FOR CY 1975 AS A WHOLE THE TRADE SURPLUS WILL BE SLIGHTLY LOWER THAN THE HIGH ANNUAL RATE IN RECENT MONTHS.

5. FINATT AGREES WITH OECD ASSESSMENT THAT JAPAN WILL CONTINUE TO INCREASE ITS EXPORT MARKET SHARES. EXPORTS TO MID-EAST AND COMMUNIST COUNTRIES HAVE DOUBLED IN FIRST 10 MONTHS OF 1974. TRADE WITH SEASIA COUNTRIES IS NOW SOFTENING UNDER IMPACT OF SLOWDOWN IN THOSE ECONOMIES AND IN THEIR EXPORT GROWTH. SHARE OF EXPORTS TO U.S. HAS CHANGED LITTLE FROM 23.1 PERCENT IN FIRST HALF TO AVERAGE OF 23.2 PERCENT FROM JULY-NOV, WHEREAS U.S. IMPORT SHARE RECOVERING IN RECENT MONTHS, REACHING 21.5 PERCENT IN OCT-NOV. AS VALUE OF IMPORTS HAS RECEDED SOMEWHAT.

FORECAST: IN BILLIONS OF DOLLARS

	CY 1974 ESTIMATE	CY 1975 FORECAST
EXPORTS	54.5	66.2
IMPORTS	MINUS 52.7	59.7
TRADE BALANCE	1.8	6.5
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SERVICES AND TRANSFERS	MINUS 6.2	MINUS 6.5
CURRENT ACCOUNT	MINUS 4.4	0
L-T CAPITAL	MINUS 4.0	

BASIC BALANCE MINUS 8.4

OVERALL BALANCE MINUS 7.0

OFFICIAL SETTLEMENTS

BALANCE 1.8

6. CONTINUED STABILITY FO THE YEN/DOLLAR RATE WOULD BE
CONSISTENT WITH THE PROSPECT OF LITTLE CHANGE IN JAPAN'S
PAYMENTS POSITION ON CURRENT ACCOUNT. GOJ NOW REALIZES
RATE MOVEMENT IS DOUBLE-EDGED (I.E. DEPRECIATION MAY HELP EXPORTERS
BUT HURT ANTI-INFLATIONARY POLICY) AND CAPITAL DLOWS DO
AFFECT RATE MOVEMENTS. JAPAN HAS AMBITIOUS LONG-TERM
FOREIGN INVESTMENT COMMITMENTS AND PLANS WHICH WILL HAVE
TO BE MATCHED BY EQUIVALENT AMOUNT OF OVERSEAS FINANCING.
NEVERTHELESS, JAPAN REMAINS IN STRONG EXTERNAL BORROWING
POSITION COMPARED WITH OTHER DEVELOPED COUNTRIES.
HODGSON

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC CONDITIONS, ECONOMIC DATA
Control Number: n/a
Copy: SINGLE
Draft Date: 24 DEC 1974
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: ShawDG
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1974TOKYO16689
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: D740373-0834
From: TOKYO
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1974/newtext/t19741211/aaaaajan.tel
Line Count: 296
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION TRSE
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 6
Previous Channel Indicators:
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: n/a
Review Action: RELEASED, APPROVED
Review Authority: ShawDG
Review Comment: n/a
Review Content Flags:
Review Date: 31 JUL 2002
Review Event:
Review Exemptions: n/a
Review History: RELEASED <31 JUL 2002 by worrelsw>; APPROVED <25 MAR 2003 by ShawDG>
Review Markings:

Declassified/Released
US Department of State
EO Systematic Review
30 JUN 2005

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: ECONOMIC FORECAST FOR JAPAN 1975 SUMMARY: IN ANSWER TO SPECIFIC TREASURY REQUEST, FOLLOWING
TAGS: EFIN, JA
To: STATE
Type: TE
Markings: Declassified/Released US Department of State EO Systematic Review 30 JUN 2005